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CRS Issue Brief for Congress

Military Retirement: Major Legislative Issues

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Military Retirement: Major Legislative Issues

SUMMARY

The military retirement system includes benefits for retirement after an active or reserve military career, disability retirement, and survivor benefits for eligible survivors of deceased retirees. A variety of major changes in military retirement were enacted in the FY2000 National Defense Authorization Act (P.L. 106-65, October 5, 1999), including the following:

Repeal of military retirement cuts enacted in mid-1986, which would have been effective for persons first retiring in mid-2006. These cuts (known as "Redux") were adopted primarily to save money, create a more experienced career force, and enable the military to manage its career force better. However, some believed that Redux was contributing to the loss of too many career people. Military personnel now have the option of retiring under Redux and receiving a cash bonus of $30,000 or of retiring under the more generous pre-Redux formula.

Allowing military personnel to invest in the civil service Thrift Savings Plan (TSP). Under the TSP, a portion of a military member's pay is deposited into a tax-deferred account where the funds are held in trust and invested, to be withdrawn at retirement. Adopting such a plan gives military personnel a retirement benefit available to civilians and enables military personnel to share in the long-term rise in equity markets. However, some opponents suggested its existence would provide an excuse for later cuts in other retirement benefits. Military personnel are now allowed to enroll in the federal civil service TSP, but a variety of problems have slowed its actual implementation. Implementation appears more likely now, however, due to agreement in Congress to earmark funds in the FY2001 congressional budget resolution to fund the military TSP program. Provisions to authorize it in FY2001 are contained in both the House and Senate Armed Services Committee versions of the FY2001 defense authorization bill.

Authorization of a special pay for certain military retirees eligible to receive both military nondisability retired pay and VA disability compensation. Current law provides that military retired pay be reduced by the amount of VA disability compensation. Some maintain this is inequitable and unfair; it has been defended on grounds of cost and of the need to avoid setting a precedent for concurrent receipts of numerous other benefits. A provision of the FY2000 National Defense Authorization now authorizes some retirees to receive a special payment, in effect a *de facto* kind of concurrent receipt, although the actual law banning concurrent receipt is still in effect. Some recent assertions that there is a "windfall," or "surplus" in the Military Retirement Fund which could pay for some concurrent receipt costs are not valid; they are based on an incorrect understanding of how the amount of money in the Fund is determined. On June 7, 2000, a floor amendment by Senator Reid to the FY2001 defense authorization bill, which would completely repeal the offset and allow full concurrent receipt, was passed.

MOST RECENT DEVELOPMENTS

*On June 9, 2000, a floor amendment by Senator Reid (*S.Amdt. 3198*), to the FY2001 National Defense Authorization Act, which would allow full concurrent receipt of military nondisability retired pay and VA disability compensation, passed the Senate.*

BACKGROUND AND ANALYSIS

Military Retirement: Key Elements and Issues

Military Retirement: Program Summary

In FY2001, total federal budget outlays for military retirement will be an estimated $34.0 billion and DOD budget outlays will be an estimated $11.4 billion. (The differing figures for total federal and DOD outlays result from the use of the accrual method in accounting for the costs of military retirement. See the section below on Cost Data for a discussion of accrual accounting.) **Table 1** shows the estimated numbers of retirees and costs of their retired pay for FY1999-FY2001.

Table 1: DOD Retired Military Personnel and Survivors: Estimated Numbers and Costs, FY1999-FY2001

	Total	Retirees from an Active Duty Military Career	Disability Retirees	Reserve Retirees	Survivor Benefit Recipients
FY2001	1,968,000/ $34.00 billion	1,363,000/ $28.17 billion	102,000/ $1.35 billion	225,000/ $2.42 billion	278,000/ $2.02 billion
FY2000	1,957,000/ $33.01 billion	1,358,000/ $27.35 billion	105,000/ $1.37 billion	228,000/ $2.39 billion	266,000/ $1.90 billion
FY1999	1,947,000/ $32.06 billion	1,356,000/ $26.52 billion	109,000/ $1.40 billion	229,000/ $2.35 billion	253,000/ $1.79 billion

Sources: Office of the Actuary. Department of Defense. *Valuation of the Military Retirement System. September 30, 1998*: K-8, K-10, K-14, K-16, L-2, and L-4.

"Redux": Its 1986 Enactment and 1999 Repeal

Conceptual Issues. For more than 30 years, the military retirement system has been the object of intense criticism and equally intense support among military personnel, politicians, and defense manpower analysts. Critics of the military retirement system have periodically alleged, since its basic tenets were established by legislation enacted in the late 1940s, that it costs too much, has lavish benefits, and contributes to inefficient military personnel management. Others have strongly defended the existing system–in particular, its central feature of allowing career personnel to retire at any age with an immediate annuity upon completing 20 years of service–as essential to recruiting and maintaining sufficient high-quality career military personnel who could withstand the rigors of wartime service if necessary. Cuts in retired pay for future retirees were enacted in the Military Retirement Reform Act of 1986 (P.L. 99-348, July 1, 1986; the "1986 Act," now referred to frequently as the "Redux" military retirement system). Although enactment of Redux in 1986 represented a success for those who argued that the pre-Redux system was too generous, the repeal of compulsory Redux in late 1999 by the FY2000 National Defense Authorization Act indicated that those who defend the pre-Redux system are once again ascendant.

Debate over the effects of Redux–or any similar change in a pension-type entitlement program–were hampered by the simple fact that it was impossible to predict in advance all the factors influencing the future decisions of career military personnel to retire. It was therefore equally difficult if not impossible to disaggregate Redux' effects from those of other factors affecting members' retirement decisions. The basic fact that Redux did represent a cut in benefits led many to assume it would have a negative effect; others, noting that the Act did attempt to positively change the relative worth of later years of service, suggested that it might have an overall positive effect.

In 1994, a Rand Corporation study found that the 1986 Act would make career officers 10% less likely, in collective terms, to serve at least a 20-year career until retirement; enlisted personnel were predicted to be even more adversely affected, at 20%. A 1987 CRS report by the author of this issue brief, using DOD's own econometric models, found that such detrimental effects could also occur, in some categories of military personnel (CRS Report 87-702, *The Military Retirement Reform Act of 1986: Issues and Implications*; out of print, but copies may be obtained from this author). A March 1999 Congressional Budget Office (CBO) study of Redux had mixed results. In strict quantitative terms, the study states that "The analysis, based on the retention patterns of the first groups to be covered by the REDUX system, finds that the retirement changes enacted in 1986 appear to be having little effect on the midcareer retention of officers or enlisted personnel." However, it did note that Redux could have a greater effect in the future, and it explicitly observed that the symbolic effect of Redux and/or its repeal at the current time could have a great effect on career retention.

The Repeal of Redux, 1997-1999. Congress began taking notice publicly of potential problems related to Redux in 1997, well before the executive branch addressed the issue. During the fall of 1998, the Administration announced that it supported Redux repeal. Eventually, the FY2000 National Defense Authorization Act contained provisions for repealing compulsory Redux; it allows post-August 1, 1986 entrants to retire under the pre-Redux system or opt for Redux plus an immediate $30,000 cash payment(see below).

Entitlement to Retired Pay and Retired Pay Computation Base

A service member becomes entitled to retired pay upon completion of 20 years of service, regardless of age. (The average nondisabled enlisted member retiring from an active duty military career in FY1998 was 41 years old and had 21 years of service; the average officer was 46 years old and had 23 years of service.) A member who retires from active duty is paid an immediate monthly annuity based on a percentage of his or her retired pay computation base. For persons who entered military service before September 8, 1980, the retired pay computation base is final monthly basic pay being received at the time of retirement (basic pay is one component of total military compensation, comprising approximately 65%-75% of the total depending on the service member's entitlements to various special pay, bonuses, and other entitlements). For those who entered service on or *after September 8, 1980*, the computation base is the average of the highest 3 years (36 months) of basic pay.

Retired Pay Computation Formula

Military Personnel Who First Entered the Service before August 1, 1986. All military personnel who first entered military service **before** August 1, 1986, have their retired pay computed at the rate of 2.5% of the retired pay computation base for each year of service. The minimum amount of retired pay to which a member entitled to compute his or her retired pay under this formula is therefore 50% of the retired pay computation base (20 years of service X 2.5%). A 25-year retiree receives 62.5% of the computation base (25 years of service X 2.5%). The maximum, reached at the 30-year mark, is 75% of the computation base (30 years of service X 2.5%).

Military Personnel Who First Entered the Service on or after August 1, 1986. Personnel who first enter service **on or after** August 1, 1986, in accordance with the provisions of the FY2000 National Defense Authorization Act, are required to select one of two options in calculating their retired pay within 180 days of reaching 15 years of service:

Option 1: Pre-Redux. They can opt to have their retired pay computed in accordance with the pre-Redux formula, described above, but with a slightly modified COLA formula, which is less generous than that of the pre-Redux formula (see below, under COLAs).

Option 2: Redux. They can opt to have their retired pay computed in accordance with the Redux formula and receive an immediate $30,000 cash bonus.

The Redux Formula: Under Age 62 Retirees. Redux is different from the previous formula in two major ways. First, for retirees under age 62, retired pay will be computed at the rate of 2.0% of the retired pay computation base for each year of service through 20, and 3.5% for each year of service from 21-30. Under this new formula, therefore, a 20-year retiree will receive 40% of his or her retired pay computation base upon retirement (20 years of service X 2.0%), and a 25-year retiree will receive 57.5% of the computation base [(20 years of service X 2.0%) + (5 years of service X 3.5%)]. A 30-year retiree, however, will continue to receive 75% of the retired pay computation base [(20 years of service X 2.0%) + (10 years of service X 3.5%)]. The changed formula, therefore, is "skewed" much more sharply in favor of the longer-serving military careerist, theoretically providing an incentive to remain on active duty longer before retiring.

The Redux Formula: Retirees 62 and Older. Second, when a retiree reaches age 62, his or her retired pay will be recomputed based on the old formula — a straight 2.5% of the retired pay computation base for each year of service. Thus, beginning at 62, the 20-year retiree receiving 40% of the computation base for retired pay, according to the new formula, will begin receiving 50% of his or her original computation base; the 25-year retiree's annuity will jump from 57.5% of the original computation base to 62.5%; and the 30-year retiree's annuity, already at 75% of the original computation base under both the old and new formulas, will not change. (Note: this change is an increase in monthly retired pay, not a lump sum at age 62.)

Military Retired Pay and Social Security

Military personnel do not contribute a percentage of their salary to help pay for retirement benefits. They have paid taxes into the social security trust fund since January 1, 1957, and are entitled to full social security benefits based on their military service. Military retired pay and social security are not offset against each other; military retirees receive full social security benefits in addition to their military retired pay.

Retired Pay and Survivor Benefit COLAs

Military retired pay is protected against inflation by statute (10 USC 1401a). The Military Retirement Reform Act of 1986, in conjunction with the recent changes in the FY2000 National Defense Authorization Act, provides for COLAs as follows (**the most recent COLA, that of January 1, 2000, was 2.4%**):

Pre-August 1, 1986 Entrants

For military personnel who first entered military service before August 1, 1986, each December a cost-of-living-adjustment (COLA) equal to the percentage increase in the Consumer Price Index (CPI) between the third quarters of successive years will be applied to military retired pay for the annuities paid beginning each January 1. For example, assume that the Consumer Price Index rises from 400.0 in September 2005 to 412.0 in September 2006, an increase of 12.0 points or 3.0% of 400.0. The monthly retired pay that accrues during December 2006, and will actually be paid to retirees on January 1, 2007, would be increased by 3.0% above that amount paid the previous month.

Entrants on or after August 1, 1986

For those personnel who first entered military service on or after August 1, 1986, the FY2000 National Defense Authorization Act provides that their COLAs will be calculated in accordance with either of two methods, as noted below.

Non-Redux Recipients. Those personnel who opt to have their retired pay computed in accordance with the pre-Redux formula will have their COLAs computed as described above for pre-August 1, 1986 entrants.

Redux/$30,000 Cash Bonus Recipients. Those personnel who opt to have their retired pay computed in accordance with the Redux formula, and receive the $30,000 cash bonus, will have their COLAs computed as follows. Annual COLAs will be held to one percentage point below the actual inflation rate for retirees under age 62. Retirees covered by this new COLA formula would thus receive a 2.0% increase (rather than 3.0%) in their military retired pay under the hypothetical example described in the above paragraph. When a retiree reaches age 62, there will be a one-time recomputation of his or her annuity to make up for the lost purchasing power caused by the holding of COLAs to the inflation rate minus one percentage point. This recomputation will be applied to the old, generally more liberal retired pay computation formula on which retirees 62 or older will have their annuities computed (see the above subsection entitled Retired Pay Computation Formula), compounding, for most retirees, the size of this one-time annuity increase. After the recomputation at 62, however, future COLAs will continue to be computed on the basis of the inflation rate minus one percentage point.

Other Legislative Issues Regarding Military Retirement

A MilitaryThrift Savings Plan

A MilitaryThrift Savings Plan (TSP): Background. Because of their rapid growth in the civilian sector, beginning in the mid-1990s, many within and without DOD urged that military personnel be authorized a "defined contribution" element of their total retired pay, as is the case for federal civil servants and many private-sector employees. A defined contribution retirement plan is essentially a savings plan with a separate account maintained by the employer for each employee. Under such a plan, the employee bears much of the risk of investment decisions for his or her account, and consequently the amount of retired pay or pension cannot be predicted with certainty. A defined benefit retirement plan follows the more traditional model of a worker being entitled to retired pay or pension based on a computed formula according to years of service and salary, and the worker knows with certainty what the ultimate amount of his or her retired pay will be.

Under a defined contribution plan, a portion of current salary is deposited into tax-deferred individual accounts where the funds are held in trust and invested for their retirement. The defined contribution plan for federal civil servants is referred to as the Thrift Savings Plan (TSP). Such plans are called "401(k)" plans (the reference is to the section of the Internal Revenue Code) in the private sector. (The Rand Corporation, under contract to the Office of the Secretary of Defense, has recently prepared a study of how to integrate a defined-contribution element into military retirement. See Beth J. Asch, Richard Johnson, and John T. Warner. *Reforming the Military Retirement System*. Santa Monica, CA, National Defense Research Institute, Rand Corporation, 1998. 81 p.)

Allowing Military Participation in the Federal Civil Service TSP. The FY2000 National Defense Authorization Act authorizes military personnel to contribute to the civil service TSP (see Subtitle F, Sections 661-63, S. 1059; H.Rept. 106-301). The FY2000 Act allows military personnel to contribute up to 5% of their total basic pay (basic pay is one element of total military compensation, which usually amounts to about 65-70% of the total for most military personnel), plus taxable bonuses and special pays, into a tax-deferred account. Each individual military service will be allowed to offer matching contributions as a retention incentive, in exchange for a commitment from the service member to serve six years on active duty in a particular occupational skill. Reserve (including National Guard) personnel could participate in the TSP in the same fashion as active duty personnel. Existing Internal Revenue Code limits on how much money can be deposited yearly would apply to military personnel as it does now to civil servants–the current limit is $10,500.

Funding the Military TSP. A variety of problems slowed the implementation of the military TSP after its enactment in 1999. Because its implementation will reduce tax receipts to the Treasury, DOD had to find offsetting cuts in existing federal entitlement programs before the program could begin operation. The 1999 TSP statute contained no such cuts. Nor did the Administration's FY2001 defense budget. This issue appears to have been solved, at least on the Senate side, by the announcement on April 6, 2000, by Senators Warner, Armed Services Committee Chairman, and Domenici, Budget Committee Chairman, that money would be earmarked from the projected budget surplus to fund the TSP in FY2001.

Authorizing Legislation. Authorizing language allowing the program to proceed will be in the forthcoming FY2001 National Defense Authorization Act. The House Armed Services Committee version of the FY2001 National Defense Authorization Act, reported May 12, 2000 (H.Rept. 106-616), provides that the TSP for military personnel will actually begin operating on July 1, 2001 (Section 651, H.R. 4205). The Senate Armed Services Committee bill, reported May 4 (S.Rept. 106-292), will allow operations to begin 180 days after enactment of the bill (Section 643, S. 2549).

Administrative Costs for Reserve TSP Participation. Another issue with starting the TSP related to the effects of reserve participation in the TSP on administrative costs. Because reservists receive so much less pay than active duty personnel over the same period of time, extension of the TSP to reservists will result in a large number of TSP accounts with comparatively very small balances. The administrative costs of each of these accounts will, however, be the same as for accounts with much larger balances. The agency that administers the TSP–the Federal Retirement Thrift Investment Board–stated that in order to pay for the reserve administrative costs, it would have to charge both active duty and reserve military participants in the TSP a much larger amount than it charges federal civil servants–or that it would charge active duty participants alone if reservists were not entitled to participate. (The Board intends to charge active duty personnel one percent of their account balance per year and reservists six percent, compared with the much smaller civilian administrative charge of six dollars per $1,000 in the account.) However, in early May the TSP board agreed not to charge higher administrative costs to reservists, so this issue appears to have been resolved.

Repeal of Dual Compensation Laws

The Dual Compensation Act of 1964 (P.L. 88-448, Act of August 19, 1964; 78 Stat. 484) had required retired regular officers of the armed forces to forfeit some of their retired pay (currently the amount remaining after the first $10,450.77 plus half of the remainder are subtracted from the gross annual pay being received) if they were employed by the federal civil service after retirement. The Civil Service Reform Act of 1978 (P.L. 95-454, 92 Stat. 1111) required all military retirees (not just retired regular officers) to forfeit that portion of their retired pay which, when added to their civil service pay, brought the total for the two above Level V of the Executive Schedule for civil service pay, currently $110,700 annually. These restrictions were known as dual compensation, or more colloquially "double-dipping." Both types of restrictions were completely repealed by Section 651 of the FY2000 National Defense Authorization Act.

Concurrent Receipt of Military Retired Pay and VA Disability Compensation

Current law requires that military retired pay be reduced by the amount of any Department of Veterans Affairs (VA) disability compensation received. For several years some military retirees have sought a change in law to permit receipt of all or some of both, and legislation to allow this has been introduced during the past several Congresses. This issue is frequently referred to as "concurrent receipt," because it would involve the simultaneous receipt of two types of benefits. The FY2000 National Defense Authorization Act authorized what is in effect a *de facto* concurrent receipt provision for severely disabled military retirees. Monthly payments of $100 would be authorized for military retirees with 70 or 80% disability; $200 for 90% disabled retirees; and $300 for 100% disabled retirees, if the disability rating is received from the VA with four years of retiring from military service (Sec. 658 of the FY2000 Act). The existing concurrent receipt restrictions remain in effect, however. The special pay is taxable, and DOD anticipates being able to begin paying it to eligible individuals by March 1, 2000, for recent retirees, and then progressively bringing earlier retirees into the system on April 1 and May 1, 2000. For all individuals, payment will be retroactive to October 1, 1999. Eligible personnel need not apply for the pay; their eligibility will be identified by DOD and VA computers automatically. For further discussion of this issue, see CRS Report 95-469, *Military Retirement and Veterans' Compensation: Concurrent Receipt Issues.*

Action in the 2nd Session, 106th Congress, on Concurrent Receipt. On June 7, 2000, during debate on the FY2001 National Defense Authorization Act, the Senate passed a floor amendment by Senator Reid which would allow full concurrent receipt of military retired pay and VA disability compensation – no offset of one against the other would remain. Presumably, if enacted into law, this would be accompanied by a repeal of the concurrent-receipt related "special pay" described in the preceding paragraph.

The Alleged "Surplus" in the Military Retirement Fund and Concurrent Receipt. Recent assertions in March and April 2000 that there is a "windfall" or "surplus" in the Military Retirement Fund, which could be used to help pay for allowing some military retirees to receive their military nondisability retired pay and VA disability compensation concurrently are incorrect. They are based on an invalid assumption about how the amount of money in the Fund is determined. Complicated calculations are used to compute the amount of money which has to be transferred to the Military Retirement Fund from the DOD budget (see the section immediately below on "Military Retirement Budgeting and Costs") to pay for future retirement costs. These calculations do, in fact, include projections, based on past experience, on how many military retirees will probably be eligible for VA disability compensation as well as military retired pay–and, therefore, how much less retired pay the Fund will have to pay out to retirees because they are getting VA compensation instead. The idea of the "windfall" assumed that the calculations did not take the VA compensation offset into account.

Military Retirement Budgeting and Costs

Accounting for Military Retirement in the Federal Budget

All DOD budgets through FY1984 reflected the costs of retired pay actually being paid out to personnel who had already retired. Congress simply appropriated the amount of money required to pay current retirees each year. Since FY1985, the "accrual accounting" concept has been used to budget for the costs of military retired pay. Under this system, the DOD budget for each fiscal year reflects the estimated amount of money that must be set aside and accrued at interest – actually, invested in special, non-marketable U.S. government securities similar in some ways to Treasury bills and bonds – to fund the retired pay to which persons currently in the Armed Forces during that fiscal year, and who ultimately retire, will be entitled in the future. These estimated future retirement costs are arrived at by making projections based on the past rates at which active duty military personnel stayed in the service until retirement, and on assumptions regarding the overall U.S. economy, such as interest rates, inflation rates, and military pay levels. These DOD budget outlays for retirement are computed as a percentage of a fiscal year's total military pay costs for each military service. Approximately 35-40% of military basic pay costs must be added to the DOD personnel budget each fiscal year to cover the future retirement costs of those personnel who ultimately retire from the military.

DOD budget outlays in each fiscal year that pay for the estimated cost of future retirees are transferred in a paper transaction to a Military Retirement Fund, located in the Income Security Function of the federal budget. The Military Retirement Fund also receives [paper] transfers from the General Fund of the Treasury to fund the initial unfunded liability of the military retirement system. This is the total future cost of military retired pay that will result from military service performed prior to the implementation of accrual accounting in FY1985. Money is disbursed from this Military Retirement Fund to current retirees. Individual retirees continue to receive their retired pay from DOD finance centers. Technically, however, because this money paid to individuals comes not from the DOD budget, but from the Fund, it is paid out by the Income Security function of the federal budget. Actual payments to current retirees thus show up in the federal budget as outlays from the federal budget as a whole, but not from DOD. Under accrual accounting, therefore, total federal outlays for each fiscal year continue to reflect only costs of payments to military members who have already retired, as was the case before accrual accounting began. Accrual accounting only changes the manner in which the federal government accounts for military retired pay; it does not affect actual payments to individuals in any way.

Unfunded Liability

Current debates over both federal civilian and military retirement have included some discussion of the "unfunded liability" of both. As noted above, the military retirement system's unfunded liability consists of future retired pay costs incurred before the creation of the Military Retirement Fund in FY1985. These obligations are being liquidated by the payment to the Fund each year of an amount from the General Fund of the Treasury, and will be fully paid, based on current calculations, by FY2043. The unfunded liability at the end of FY1998 was $499.5 billion.

Concerns have been voiced about the size of the unfunded liability within Congress; some suggest it is a huge bill coming due that will eventually force major increases in federal spending. However, (1) the hundreds of billions of dollars of unfunded liability represents a cumulative total to be paid out to retirees over approximately the next 50 years, not all at once (private pensions can come due all at once if a company goes out of business and has to pay off its pension liabilities immediately); (2) by the time some persons first become eligible for retired pay under the pre-accrual accounting system, many others will have died; and (3) unlike the private sector, there is no way for employees to claim immediate payment of their future benefits. An analogy would be the mortgage on a house. Most homeowners cannot afford to pay cash for a house, so they get a mortgage. If the mortgage had to be paid in full, almost no homeowners could afford to do so. However, spread out over 30 years, or a smaller period, the mortgage payments are affordable. Similarly, the unfunded liability of federal retirement programs is affordable when federal retired pay/pension outlays are spread over several decades.

Military Retirement Cost Trends

Because military retirement is an entitlement paid to individuals, rather than a discretionary program, the retirement costs to the *total federal budget* (payments to current retirees and survivors) always rise modestly each year, to deal with an easily- predictable slow rise in the number of retirees and survivors. The cost to the DOD budget (estimated future retirement costs of current active and reserve personnel) declined after FY1989 (the beginning of the post-Cold War drawdown), as the size of the force — and hence, the number of people who will retire from it in the future — declined. However, as the drawdown stabilized, so did the DOD budget costs of retirement. The repeal of the mandatory Redux retirement cuts in 1999, however, will result in the DOD retirement costs rising again, by some estimates up to $2 billion per year, depending on how many post-2006 retirees elect to retire under Redux and take their $30,000 cash bonus, or forego the bonus and retire under the more generous non-Redux formula.

Tables 2 and 3 indicate the costs of military retired pay in terms of both federal budget outlays (payments to current retirees) and Department of Defense accrual outlays (money set aside to fund future retirees).

Table 2. Military Retirement: Total Federal Budget Outlays
(billions of current dollars)

Requested FY2001	$34.0
Estimated FY2000	33.0
Actual FY1999	32.1
Actual FY1998	31.1
Actual FY1997	30.2

Table 3. Military Retirement: Accrual Outlays From DOD Budget
(billions of current dollars)

Requested FY2001	$11.4
Estimated FY2000	11.5
Actual FY1999	10.4
Actual FY1998	10.4
Actual FY1997	11.1

Costs of Repealing Redux

Total Federal Budget Costs. Because of the nature of accrual accounting, as described above, repealing the 1986 Act/Redux will have different effects on the defense budget and the total federal budget. Because, with the exception of a very few disability retirees, virtually nobody has retired, or will retire, under Redux until 2006, the costs to *the total federal budget* of the repeal of compulsory Redux will be infinitesimal until FY2008, because total federal budget costs involve the actual payments the government makes to retirees. The Congressional Budget Office (CBO) has estimated that the repeal of Redux will cost only about $1 million in increased payments to disability retirees in FY2000; and an equally small $12 million over the period FY2000-FY2005. Even by FY2010, annual costs to the total federal budget will only be $125 million.

DOD Budget Costs. On the other hand, because the DOD budget pays for the future costs of current retirees under accrual accounting, the amount of money that will have to be transferred from the DOD budget to the Military Retirement Fund to fund future retirement costs will go up immediately, because the amount transferred will have to reflect the repeal of Redux for those future retirees. CBO has estimated that the repeal of Redux embodied in S. 4 as passed by the Senate — and, by inference, the Redux repeal as enacted into law — will result in increased DOD budget costs of $674 million in FY2000 and $8.2 billion during FY2000-2005. The Administration had earlier estimated that costs of its partial Redux repeal would be $796 million in FY2000 and $6.0 billion during FY2000-FY2005. Why the Administration estimated its *partial* repeal of Redux would cost more than what CBO says the cost will be of *complete* repeal of Redux is not clear. The rationales are doubtless embodied in different economic assumptions and/or different baselines for estimate cost increases.

Unfunded Liability Costs. CBO estimated that repeal of Redux as embodied in S. 4 will result in the total unfunded liability of the military retirement system rising by $4.5 billion, or slightly less than 1% of the current total unfunded liability of the system of about $500 billion. To quote CBO on the implications of this increase, "Under current practices, the Treasury would pay the trust fund that amount over many years, but those intragovernmental transfers would have no net budgetary impact. The [total federal] budgetary impact would occur as outlays from the trust fund (direct spending) when the benefits traceable to the liability would be paid to retirees or survivors."

Costs of other Military Retirement Provisions in 1999 Legislation

Thrift Savings Plan Costs. The Joint Committee on Taxation has estimated that allowing military personnel to participate in the federal civilian TSP will result in $11 million in direct spending in FY2000, and a total of $993 million through FY2009 — or about $100 million annually. Allowing reservists to participate in the TSP will presumably increase these already-small figures slightly.

Costs of Repealing the Dual Compensation Laws. Because it originated as a floor amendment, there are as yet no formal cost estimates of the increased expenditures resulting from ending the forfeiture of some military retired pay by affected retirees. However, cost estimates for dual compensation were prepared for the Congressional Commission on Service Members and Veterans Transition Assistance in 1997. These showed that in FY1997, the retired-regular-officer pay offset saved the government (or cost retirees) about $176 million, and the Executive Schedule V pay cap saved (or cost retirees) about $28.2 million, or a total of about $204 million.

Costs of Concurrent Receipt of Military Retired Pay and VA Disability Compensation. Depending on the extent of concurrent receipt allowed, past cost estimates have varied from an annual level of about $50 million (allowing concurrent receipt for people who are rated by the VA as 100% combat-disabled) to over $2 billion (allowing concurrent receipt for all individuals eligible for both types of benefits). There have been rough estimates, based on numbers of military retirees who are 70% or more disabled and have received their disability ratings no more than four years after retirement, that the costs of the provisions likely to be in the FY2000 defense authorization will be in the $40-$60 million a year range. However, this proposal has not yet been formally costed out by either DOD or the Congressional Budget Office. As noted above, the Senate passed a floor amendment to the FY2001 defense authorization bill which would allow full concurrent receipt; presumably the cost of this would be in the approximate $2 billion yearly range which has been mentioned in the past.

Key Issues

Should Redux Have Been Repealed?

Arguments FOR Repeal of Redux.

- Relying solely on highly technical econometric studies to determine if Redux would have negatively affected retention or not was superficial. Even if such studies had showed that Redux had not yet greatly affected retention, there was enormous impressionistic evidence that it would do so, and indications from recent unpublished data from the military services that concern over retirement benefits and Redux had been rising steadily over the past several years.

- The savings that would have resulted from the original 1986 enactment of Redux would have been minuscule compared to the negative effects on career retention, which would have to have been offset by increasing other forms of compensation if sufficient quality personnel were to have been retained in the career force. Furthermore, the unprecedented circumstances of a budget surplus would have been available to help cope with the cost of repealing compulsory Redux.

- The costs of repealing Redux are low. Costs to the DOD budget will be in the range of about $2 billion yearly out of a DOD budget of $260-$300 billion over the next several years; costs to the total federal budget — those costs which affect the overall deficit, or surplus, picture, will be a few hundred million yearly until 2010 and later.

- Comparisons with civilian retirement systems are irrelevant. Military service involves unique levels of hardship and stress. Those civilian occupations, such as law enforcement or firefighting, which demand somewhat similar stresses (although far less intense than a war situation in terms of family separation and lack of creature comforts) have similar liberal early retirement provisions in their pension systems.

- Claims that the pre-Redux system led to "excessive" retired pay are misleading. The average enlisted retiree, as well as most officer retirees, is incapable of supporting a family on retired pay alone. Further, there is evidence that the salaries paid military retirees in the civilian work force are depressed when compared to non-retirees.

- Adjustments needed to lengthen the careers of a very few officers, so as to provide them with the experience and education they need for top-level assignments, can be made without making wrenching, benefit-cutting changes to the whole military retirement system.

- Redux had become, and still is, a crucial symbol. The Administration and the leadership in both parties in Congress ended up supporting repeal. Not to do so would have had a catastrophic effect on career military people, sending a message that Congress cared little indeed about the welfare of career members.

Arguments AGAINST Repeal of Redux.

- There was no empirical evidence, at the time Congress was considering repeal of Redux in 1999, that the retention behavior of military personnel had yet been affected by Redux. A Congressional Budget Office analysis of March 2, 1999, based on a statistical study of several thousand military personnel, divided among those whose retired pay is to be computed by Redux or pre-Redux formulas, found "that the retirement changes enacted in 1986 appear to be having little effect on the midcareer retention of officers or enlisted personnel."

- Redux would have saved money. A total of $2 billion per year for compulsory Redux would not have been immense when compared to the total DOD budget, but it could have bought several hundred tanks and other armored vehicles, 20 or so Air Force F-22 fighters, or several naval vessels of destroyer size.

- The Redux feature of increasing the retired pay multiplier to 3.5% for years of service past 20 might have induced more people to stay on active duty past the 20-year mark, increasing the number of experienced personnel on active duty and thereby sustaining and improving productivity.
- Given the earnings potential of skilled, capable military retirees in their late 30s or early 40s, and their ability to find remunerative civilian employment, the Redux levels of retired pay received by people with much more than 20 years of service would have beens more than ample to cushion their transition to civilian life.
- Few if any civilian retirement systems provide as high a level of benefits for people no older than the early 50s, who can voluntarily retire without regard to age.
- The only way to insure adequate levels of competence among members of the career officer corps is to lengthen their careers, enabling them to have a greater variety of, and longer, operational assignments, formal education al courses, and staff and specialized tours of duty.
- What an officer needs to know in the senior grades in the 21st Century simply cannot be "squeezed" into a career that averages 20-24 years.

Should a Thrift Savings Plan/401k Plan Have Been Created for Military Personnel?

Arguments in Support of Creating a Thrift Savings Plan for Military Personnel.

- Military personnel, like civil servants and private-sector employees, should be able to allot some of their retirement benefits to their own chosen investments.
- In particular, military personnel, because they move so often, frequently are not able to accumulate equity in a home, denying them one of the most widespread benefits of a long-term growing economy available to most civilians. Providing a contributory element to military retirement would at least partially make up for this.
- The increased portability would benefit military members who leave the service for a second career in civilian life.
- The current "cliff-vesting" attribute of military retirement — no entitlement to retired pay until reaching the 20-year mark, and eligibility for immediate retirement thereafter — is so drastic that it provides insufficient flexibility for military personnel managers in separating military members before they reach the 20-year mark.

- Some action that increases military retirement options and pay is imperative in an era where current career personnel who entered service on or after August 1, 1986, are facing retired pay levels substantially lower than they would have received had they been able to enter the armed forces earlier.

Arguments Against Creating a Thrift Savings Plan for Military Personnel.

- The portability of a savings plan, and the fact that contributions to it would "vest" — become an entitlement to future benefits — military personnel in the retirement system before the current 20-year mark, could induce too many people to leave the service early, perhaps requiring either massive increased expenditures in current compensation or accepting huge losses of career members.

- Such career decisions might be more likely to take place in anticipation of or during a contingency operation or deployment where hostilities are imminent.
- A thrift savings plan could lead to a de facto cut in retired pay, if a smaller proportion of the total retirement compensation available to individuals would be guaranteed without regard to individual investment decisions.

- Creation of a thrift savings plan for military personnel would be viewed as an increase in benefits by many people, including Congress, making other components of the retirement system more vulnerable to cuts.

Should Concurrent Receipt of Both Military Retired Pay and VA Disability Compensation be Allowed?

Arguments IN FAVOR of Concurrent Receipt.

- Military retired pay, it is argued, was earned for length of service; the VA disability compensation, for disability. They were therefore for two different things and did not constitute a duplication of benefits.

- If cost was an issue, partial concurrent receipt should be allowed for those most severely disabled, with combat disability, or whose benefits or total income are the least.

- VA disability compensation beneficiaries are entitled to other federal benefits; why not military retired pay?

- People receiving VA disability compensation can receive pensions from a wide variety of other sources without any offset; why target military retirees?

Arguments AGAINST Concurrent Receipt.

- The cost of full, or nearly full, concurrent receipt would be enormous — over $2 billion, according to CBO.

- To set a precedent of eliminating or reducing this offset would "be sticking the camel's nose into the tent," setting a precedent for the reduction or elimination of all kinds of similar offsets of one or more federal payments. The total cost of eliminating or even reducing a broad range of such offsets (a CRS study identified at least 25) could cost the government huge amounts of money, running into the tens of billions of dollars.

- Although some federal programs do not have an offset against VA disability compensation, there are no such offsets involving (1) disability and (2) retirement from the same job and agency where the disability occurred.

- VA disability compensation is arguably authorized on much more liberal grounds than others, and a disability can be certified many years after a person leaves active military service. Accordingly, allowing concurrent receipt could lead to a windfall for people whose VA disability appears to have had a tenuous connection with their military service.

- Concurrent receipt was never promised to those asking for it.

Legislation

S. 2549 (Warner)

FY2001 National Defense Authorization Act. Reported May 12, 2000 by Armed Services Committee (S.Rept. 106-292). S.Amdt. 3198, by Senator Reid, to authorize concurrent payment of retired pay and compensation for retired members with service-connected disabilities passed Senate June 7, 2000, by voice vote.

For Additional Reading

CRS Report 98-223. *COLAs for Military Retirees: Summary of Congressional and Executive Branch Action, 1982-1999.*

CRS Report 95-1118. *Military Retirement and Personnel Management: Should Active Duty Military Careers be Lengthened?*

CRS Report 95-469. *Military Retirement and Veterans' Compensation: Concurrent Receipt Issues.*